Press Release

Tax buoyancy improves India's fiscal position

Moderate cut in fuel taxes may still keep the deficit within budgeted target

2 November 2021

India's central government fiscal position is gradually crawling out of the precarious pandemic hit scenario in FY21, with fiscal deficit for H1 FY22 standing at 35.0% (Rs. 5.3 trn) of the budget estimate (Rs. 15.06 trn), just half as compared to an average of 70.5% of actuals recorded in the first half of preceding three years. The relatively slower build up of the fiscal deficit this year continues to reflect a robust pickup in revenue collection although the progress on the disinvesment front has continued to be lower than expectations. While the non-interest revenue expenditure has been relatively slow at 2.5%YoY in the first half, it is likely to pick up going forward along with a healthy growth in capital expenditure which has already climbed by 38.3%YoY. A scenario analysis undertaken by Acuité reveals that a Rs. 5 per litre reduction in excise duty on petrol and diesel will imply a moderate revenue loss of around Rs 230-250 bn (~0.1% of GDP) for the remainder of FY22 and will not materially alter the fiscal print.

The total revenue receipts have been buoyed by robust tax as well as non-tax revenue collection. For H1 FY22, gross tax revenue collection witnessed a sharp growth of 64.2% YoY compared to the contraction of 21.6% seen in H1 FY21. Barring service tax collection that contracted in H1 FY22, all other key tax sources recorded healthy growth, with impressive growth seen in customs followed by corporate tax collections (Chart 1). Despite the supportive statistical base of last year, gross tax revenue collection as compared to the BE already stands at 53.6% in H1 FY22 (vs. 35.6% of actuals in the corresponding period in FY21) with custom duties, corporate tax, excise, and central GST exceeding 50% of BE. We expect the trend to continue in the second half of the current year with GST collections expected to remain above Rs. 1.1 trn supported by festive demand leading to an improvement in consumer spending. Notwithstanding some impact of increase in fuel prices on consumption of petrol and diesel, we expect the overall private consumption to see a significant recovery on the back of improved mobility. Healthy gross tax collection and relatively lower tax devolution to states has led net tax revenue in H1 FY22 to grow by 100.8% YoY from a contraction of 24.5% in H1 FY21.

Non-tax revenue also registered a healthy growth of 73.8% YoY in H1 FY22 compared to a contraction of 55.9% seen during H1 FY21. The key reason for robust performance under this category, however stems from the significantly higher than budgeted dividend from the RBI at Rs 991.0 bn, transferred in the month of May this year due to the synchronization of RBI's financial year with the Government of India.

It is encouraging to note the growth in cumulative expenditure incurred by the government in H1 FY22 amounting to Rs. 16.3 trn, i.e. 9.9% YoY vis-à-vis contraction of 0.6% YoY in H1 FY21. On BE basis, this translates into 46.7% of the full year target vis-à-vis 42.1% disbursal seen in the corresponding period in FY21. Revenue expenditure grew by 6.3% YoY (47.7% of FY22 BE) during H1 FY22 vis-à-vis an expansion of 1.0% (42.6% of FY21 actuals) seen in the corresponding period in FY21. However, non-interest revenue expenditure- a better metric to gauge the quality of spending rose merely by 2.5% YoY in H1 FY22 as compared to H1 FY21. On the other hand, it is encouraging to see a relatively healthy capital expenditure growth of 38.3% YoY (41.4% of FY22 BE) during H1 FY22 vis-à-vis a contraction of 11.6% (39.0% of FY21 actuals) seen in H1 FY21. Continued thrust on capital expenditure provides comfort and would be important for supporting the economy at a time when private investment is yet to pick up adequate momentum, at least in the near term. The central government under the scheme entitled 'Special Assistance to States for Capital Expenditure for 2021-22' has approved capital projects worth Rs 29.0 bn in 8 states while also releasing Rs 14.0 bn to these states.

For H2 FY22, we expect the revenue expenditure momentum to remain strong as all the government departments have now been permitted to spend as per their own approved budget for this year from an earlier mandate of restricting expenditure within 20% of BE FY22 in second quarter of FY22 in the wake of the second Covid wave.

On the expenditure front, as per our estimates, the combination of vaccination cost, COVID relief program, hike in DA/DR allowance, and higher fertilizer subsidy outgo (that recently got extended by Rs 287 bn to cover the upcoming rabi sowing season) would entail an additional spending of Rs 1.5-2.0 trn (0.8-0.9% of GDP) in FY22. In addition, there is a likelihood of topping up the FY22 MGNREGS budget of Rs 730 bn by an additional Rs 250 bn (0.1% of GDP) in the wake of fast pace of fund utilization amid increased demand for rural employment.

Overall, the central government's fiscal position in the current year is witnessing a significant recovery backed by healthy tax and non-tax revenue collections. Basis available trend, we expect government's tax as well as non-tax revenue outturn to likely exceed full year budget estimates by around Rs. 2.0 trn led by strong indirect tax mop-up, recovery in most of the sectors amidst unlocking of economy, and various compliance measures taken by the government.

Meanwhile, we continue to emphasize that the realization of record high disinvestment target of Rs. 1.7 trn would be crucial in managing the overall fiscal risks. The recent announcement of Air India disinvestment ia an important milestone but it is not significantly revenue accretive. The traction in case of large ticket size disinvestments, like LIC, BPCL could boost confidence further. The recently unveiled National Monetization Pipeline (NMP) is estimated to raise Rs 6.0 trn by monetizing core assets of the central government, over FY22-25 (out of which Rs 882 bn is earmarked for the current financial year). Timely execution on this front could generate additional revenue for the government.

In our base case scenario, we anticipate a fiscal slippage of around Rs. 268 bn compared to the BE figures; however, the fiscal deficit as % of GDP is likely to be marginally better at 6.6% (vs. the budget estimate of 6.8%) in FY22 taking into consideration higher nominal GDP led by higher inflation.

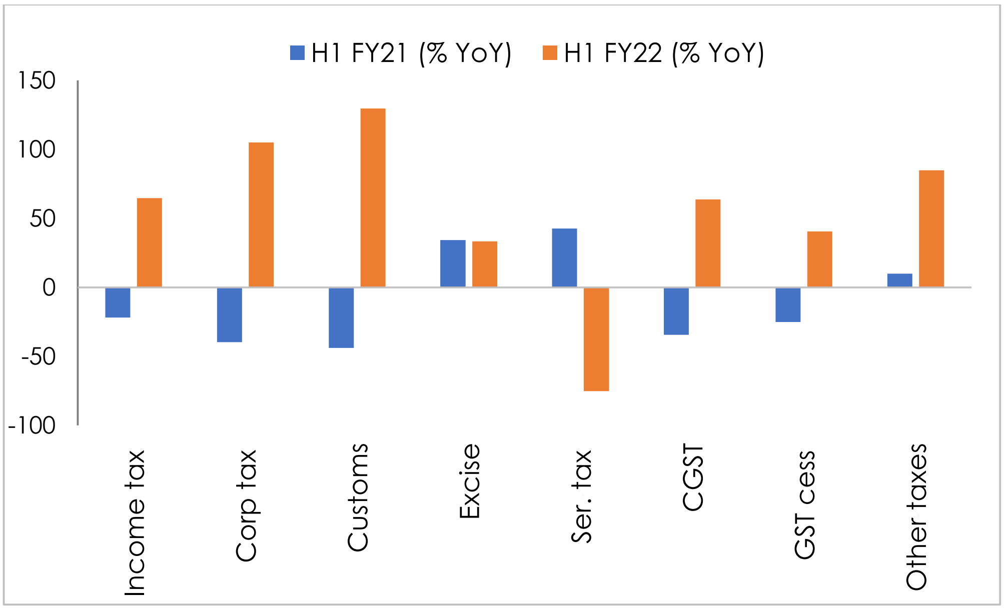
Given the backdrop of elevated domestic fuel prices feeding into India's inflation basket, there is an expectation of a moderate cut in the excise duties if the global oil prices continue to remain high. An Acuité study indicates that a Rs. 5 per litre reduction in excise duty on petrol and diesel will imply a revenue loss of around Rs 230-250 bn (~0.1% of GDP) for the remainder of FY22 to the central exchequer. Assuming a healthy pick up in fuel consumption with opening up of economy and mobility picking up in H2 FY22 we expect a gross excise collection of Rs. 4.2 trn in FY22 vis-à-vis BE of INR 3.3 trn. In our opinion, this gives the centre enough room to reduce excise duty by up to 7.5 per litre without having any major impact on its budgeted revenue expectation.

Annexure

Table1: H1 FY22 comparison of key drivers of fiscal deficit

Key Fiscal Variables (Cumulative Position as of Apr-Sep)				
	% of FY Actual/Target		% YoY	
	FY21	FY22	FY21	FY22
Revenue Receipts	33.7	60.4	-32.5	96.3
Net Tax	32.2	59.6	-24.5	100.8
Non -Tax	44.3	66.0	-55.9	73.8
Non-Debt Capital Receipts	25.4	9.6	-28.9	23.8
Total Receipts	33.5	55.6	-32.5	94.4
Revenue Expenditure	42.6	47.7	0.96	6.33
Capital Expenditure	39.0	41.4	-11.57	38.30
Total Expenditure	42.1	46.7	-0.62	9.91
Fiscal Deficit	**50.2**	**35.0**	**-**	**-**

Chart 1: Except service tax all other tax sources recorded a healthy performance



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